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ABSTRACT

This individualized, competency-based unit on dealing with legal issues, the ninth of 18 modules, is on the third level of the revised Program for Acquiring Competence in Entrepreneurship (PACE). Intended for the advanced secondary and postsecondary levels and for adults wanting training or retraining, this unit, together with the other materials at this level, emphasizes the actual application of a business plan. Five competencies are dealt with in this instructional unit, including (1) determining one's need for legal assistance, (2) selecting the provisions that one desires in a lease, (3) preparing sales contracts (such as credit sales or long-term sales) that may be utilized in one's business, (4) evaluating contracts, and (5) determining one's needs for protection of ideas and inventions. Materials provided include objectives, preparation information, an overview, content (with questions in margins that guide the students' reading), activities, assessment forms, and notes and sources. The unit requires using approximately 3 hours of class time. (YLB)

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PACE
REVISED
Program for Acquiring Competence in Entrepreneurship

UNIT 9

☐ Level 1
☐ Level 2
☑ Level 3

Dealing with Legal Issues

Developed by M. Catherine Ashmore and Sandra G. Pritz

You will be able to:

- **Determine your need for legal assistance.**
- **Select the provisions that you desire in a lease.**
- **Prepare sales contracts (such as credit sales or long-term sales) that may be utilized in your business.**
- **Evaluate contracts.**
- **Determine your needs for protection of ideas and inventions.**

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Research & Development Series No. 240 CB 9

BEFORE YOU BEGIN . . .

1. Consult the *Resource Guide* for instructions if this is your first PACE unit.

2. Read the Unit Objectives on the front cover. If you think you can meet these objectives now, consult your instructor.

3. These objectives were met at Levels 1 and 2:

   Level 1 -

   - Describe why a basic understanding of legal issues is important to the small business owner/manager
   - Define the term "contract"
   - Identify the conditions that call for a written contract
   - Name and describe the five essential components of a contract

   Level 2 -

   - Describe the major legal issues faced by entrepreneurs
   - Determine when and how to obtain assistance with legal issues
   - Identify major types of contracts used by entrepreneurs
   - Identify the major rights and responsibilities of lessees and lessors
   - Identify special contracts used by entrepreneurs (mortgage vs. deed of trust, credit sales contract, and long-term sales contract)

   If you feel unsure about any of these topics, ask your instructor for materials to review them.

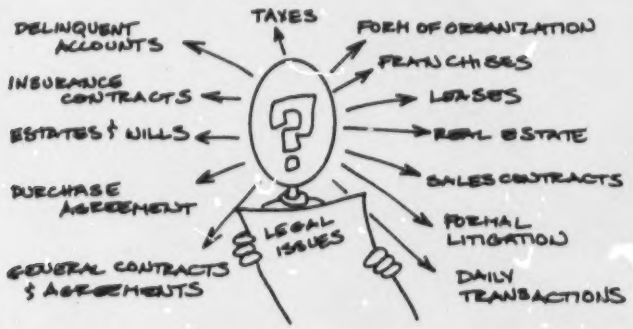
4. Look for these business terms as you read this unit. If you need help with their meanings, turn to the Glossary in the *Resource Guide*.

detriment	reasonable definiteness
fraud	service marks
patent	trademark

DEALING WITH LEGAL ISSUES

WHAT IS THIS UNIT ABOUT?

Daily involvement in sales, operations, finance, and overall management leaves the small business owner with little time to assume new responsibilities. However, the importance of the legal aspects of business cannot be neglected. The various legal points involved in day-to-day and long-term decisions related to the business must be understood. The small business owner will need to decide whether to improve his or her personal understanding of law or whether to delegate some of the responsibility to an attorney or other nonlegal adviser.



The small business owner, the key employees, or the firm's attorney will need to be able to cope with legal questions as they develop. Someone must decide whether a particular situation involves major or minor legal matters. Someone must be able to determine the degree of risk the firm faces when legal problems arise. If this skill is lacking in the business's management, serious consequences could develop later.

This unit is designed to provide the small business owner with information about what can be done to recognize and reduce legal problems. This information should help the entrepreneur deal with legal problems effectively.

Some of the questions dealt with in this unit are as follows:

- How can the small business owner recognize potential sources of legal problems?
- How can the owner reduce legal problems?
- What are some legal issues entrepreneurs face?
- Who can assist the small business owner with legal problems?
- Does the small business owner need an attorney?
- How do you select an attorney?

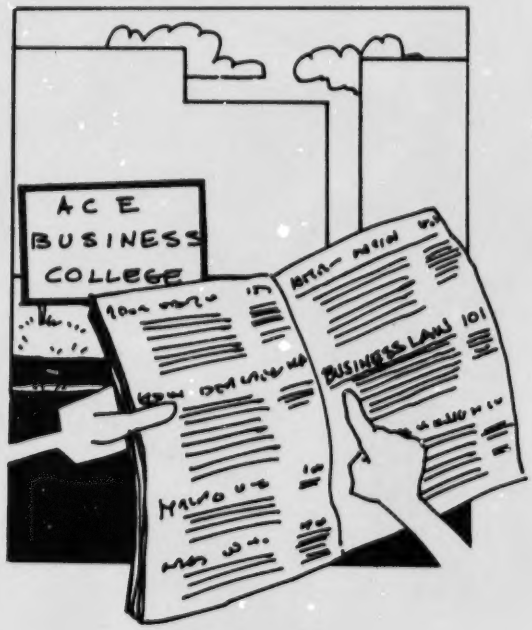
Contracts will also be discussed. Special emphasis will be placed on leases and sales contracts. You will learn what stipulations you may want in a sales contract to purchase an existing small business.

Next, you will explore information related to the various laws that will affect your business. After that, the protection of ideas and concepts through patents, trademarks, service marks, or copyrights will be discussed.

HOW CAN THE SMALL BUSINESS OWNER RECOGNIZE POTENTIAL SOURCES OF LEGAL PROBLEMS?

In certain business situations, legal aspects are involved. It may be because of the nature of the transaction, such as a special contract or bill of sale, or perhaps because of a special type of negotiable instrument. It may be a transaction requiring professional help—such as a real estate deal, bank loan, or a licensing transaction. Or it may be a situation that involves large sums of money; one on which you will want to seek legal assistance.

In any case, you will have to determine whether to handle the problem or to seek outside advice. As part of the decision, you will naturally consider the risk involved in the transaction. If it is minor, you may decide to take a chance. However, it is important to recognize all the factors before making a decision. One of the best ways to prepare to make these decisions is to take a course in business law. Almost all colleges and business schools offer such courses.



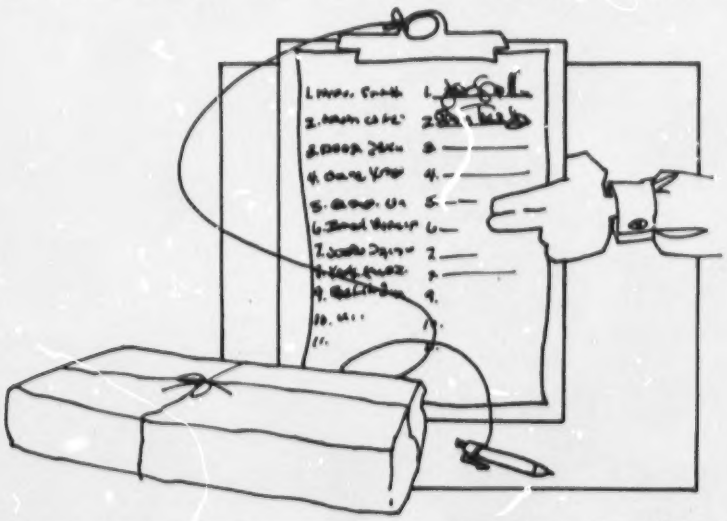
As an owner/manager, you don't have to be a lawyer, but you should be able to recognize potential legal problems that might develop from certain business situations. You should also be prepared to take the necessary steps to avoid or minimize risk. In addition, you will want to know when an attorney is needed and how to select an attorney.

The process of keeping up to date with changes in legislation and other legal issues related to small business is a difficult task. You may have little time to read about a field that is constantly changing due to court decisions and new legislation. In order to keep up to date with legal issues related to the business, you may wish to watch trade journals for articles on major legal changes that affect your industry.

You will need to try to avoid legal entanglements from any source because they are not only a strain on your firm's relations with customers and suppliers, but are also a drain on your time and on the firm's funds.

HOW CAN THE SMALL BUSINESS OWNER REDUCE LEGAL PROBLEMS?

Systems and procedures can help reduce legal problems involving customers, suppliers, employees, and others. For example, to have proof of delivery, the retailer should insist on a signature for goods. Then, should any problems develop, the business will be protected.



An entrepreneur must recognize the advantage of avoiding litigation whenever possible. This will not only save time, but will also avoid jeopardizing the firm's relationship with the many people with whom it does business.

A properly drawn agreement or contract can help avert litigation. If a matter is too small for a formal agreement, an exchange of letters may be useful. It is impractical to legalize every business transaction, but it is vital for you to put important agreements in writing.

In addition, you will need to manage the firm with discipline. You will also need to make careful decisions when facing a major legal risk. Careful decision making is also in order when contracts are signed or other written commitments are made.

As a small business owner, you should gain a basic understanding of statutes and regulations that affect your firm. However, when complex problems develop, you will want to call upon competent legal counsel or the appropriate nonlegal adviser.

WHAT ARE SOME LEGAL ISSUES ENTREPRENEURS FACE?

Legal questions appear when there are any of the following problems or conditions:

- A form of organization (sole proprietorship, partnership, or corporation)
- Taxes
- Leases
- Real estate
- Delinquent accounts
- Insurance contracts
- Estates and wills
- Purchase agreements
- Sales contracts
- Franchises
- General contracts and agreements
- Formal litigations

Daily transactions with customers, suppliers, employees, and the general public expose the small business owner to many legal risks. A small business owner must be aware of local, state, and federal laws and regulations that apply to business activities.

As a small business owner, you should also be aware of the legal problems related to the company's size, trade, and geographical area location. Ignorance of the law is not accepted as an excuse, and even licensed attorneys are not always sure of the law and its interpretation by the courts.

To avoid lawsuits (litigation)—particularly unwarranted suits—you should know exactly the extent and limit of personal and business responsibilities to suppliers, customers, employees, and others. Necessary legal documents should be prepared in such a way as to limit your exposure to liability. This will require the time of the people involved as well as the services of a skilled attorney.

In addition, it may be helpful for you to be familar with some of the sources of legal problems. The sources of legal problems have been identified in the Small Business Administration publication, *Managing for Profits.*

As a small business owner, you may wish to have the assistance of an attorney or other nonlegal adviser to help you deal with these or other legal issues. Let's take a closer look at who can assist the small business owner with problems of a legal nature.

WHO CAN ASSIST THE SMALL BUSINESS OWNER WITH LEGAL PROBLEMS?

Several individuals can assist the small business owner with legal problems. An attorney may be one of your own best resources in dealing with legal issues. At a later point in this unit, the process for selecting an attorney will be discussed.

In many problems of legal nature, the service of nonlegal advisers may be very helpful. These outside advisers may include accountants, bankers, insurance advisers, advertising or trade association staff members, real estate agents, management consultants, and business friends. Whether legal or nonlegal advisers are used, the small business owner should take advantage of the many sources of specialized skills that exist in the community. Although it may take time to establish an effective advisory group, the rewards are many and measurable.

DOES THE SMALL BUSINESS OWNER NEED AN ATTORNEY?

The entrepreneur's need for legal assistance will depend upon the nature of the small business. Highly regulated industries and businesses that use a number of contracts may need legal assistance on a daily basis. Other business firms may only need assistance occasionally. Some people recommend that legal advice be used before any business agreement is made. You—the small business owner—must determine when you need an attorney. Your decision will be based on your individual business and its particular needs.

There is one very important reason for selecting a competent attorney. A competent attorney can help you avoid personal and professional litigation. This can be a strong asset for you—the small business owner—and for your business.

Another reason for selecting a competent attorney is that an attorney can help you steer your business through the jungle of governmental regulations. In the PACE unit titled *Complying with Government Regulations*, you will have an opportunity to learn more about various government regulations and how they influence your business. However, an attorney can provide additional information about government regulations and legislation. Many times, an attorney's interpretation of various statutes can help the owner steer money into business profits.

Established businesses may require a wide variety of legal services. However, the person who is thinking of starting a new enterprise may need an attorney right away. As you learned through the PACE unit titled *Choosing the Type of Ownership*, several questions arise with a new enterprise. Should it be a sole proprietorship, a partnership, or a corporation? That PACE unit will help you answer these questions. However, an attorney can provide information that will help you be more aware of the effect of this decision on the day-to-day operation of your business.

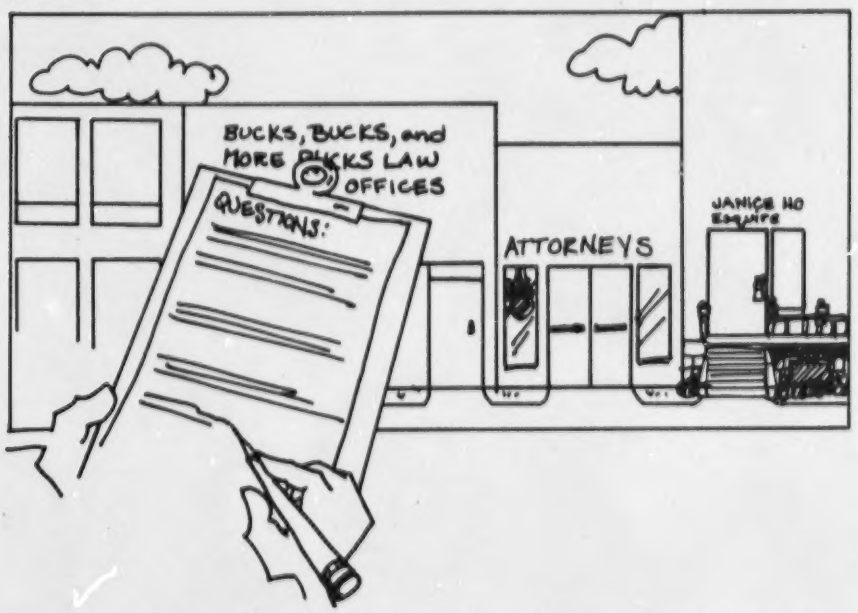
Another critical time for the business person is when a decision needs to be made to buy or rent a site for the business. If a lease is involved, this must also be examined carefully. Too often, a standard lease is signed. Afterward, the owner/manager learns that the standard lease did not fit the firm's particular circumstances. An attorney can be helpful at this point in time.

After a business has been launched, changes in marketing techniques or in technological advances may create new demands on the business. There may be a need to establish branches or divisions. Franchise arrangements might have to be worked out. An attorney can be helpful here too.

Most small businesses need money in order to operate successfully. Some firms find that they need extra working capital in order to operate. An attorney can advise when it is better for the company to go public (issue stock) or to seek conventional loans.

HOW DO YOU SELECT AN ATTORNEY?

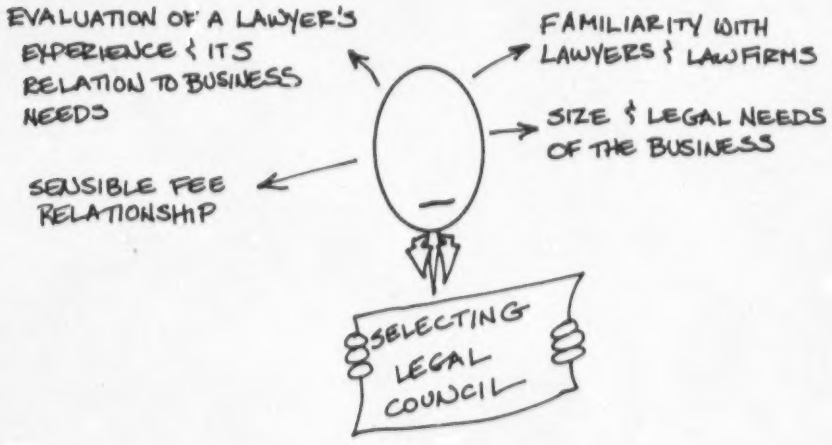
The need for good legal talent is obvious. The initial problem is where to find it. The small business owner/manager's selection of legal talent involves some consideration. In fact, several questions may arise. How should an attorney be selected? Should a large law firm having tax, labor, credit, patent, and bankruptcy specialists be retained? Should the services of a small law firm of generalists be retained, or should a lawyer who practices as an individual be retained?



The answers to these questions will depend upon several factors, including (1) the small business owner/manager's familiarity with lawyers and their firms, (2) the size and legal needs of the business, (3) an evaluation of a particular lawyer's experience and its relation to the business needs, and (4) a sensible fee relationship. Most legal firms and individual lawyers will work with a small business owner

for reasonable fees, because they expect that as the business grows so will their fees.

Attorneys who are associated with large law firms may give you a good deal of personal attention. However, the number of partners in a law firm gives you no hint of as to the range of its expertise. Some law firms, for example, concern themselves principally with criminal cases, and would be of little help in giving pertinent advice to the small business owner. On the other hand, you may find a large firm that specializes in business law that is very able to meet your needs.


EVALUATION OF A LAWYER'S EXPERIENCE & ITS RELATION TO BUSINESS NEEDS
FAMILIARITY WITH LAWYERS & LAW FIRMS
SIZE & LEGAL NEEDS OF THE BUSINESS
SENSIBLE FEE RELATIONSHIP
SELECTING LEGAL COUNCIL

A small business owner with a small or medium-sized business operation may find that the smaller law firm is very congenial and attuned to individual business needs. If a law firm has two or three partners and as many associates, chances are pretty good that their know-how will be solid and will cover a broad spectrum of issues. There are also many instances where a solo lawyer can be an excellent adviser.

Although you will find that attorneys are listed in the yellow pages, most prospective clients find their legal talent by referral. Accountants, bankers, and insurance brokers frequently are asked for recommendations; so are other businesspeople. A local judge, chamber of commerce, bar association, or legal aid society may suggest attorneys if you haven't developed extensive contacts.

Another effective way of locating an attorney is to talk with the owners of small businesses that are comparable to yours. If you elect this alternative, you may wish to ask individuals who are not direct competitors. Find out which attorneys they use and if they are satisfied with the services they have received.

Other avenues exist for locating a competent attorney. You may wish to talk with individuals who teach small business management or with law professors. Members of the Service Corps of Retired Executives (SCORE) may be helpful in identifying names of prospective attorneys for your business.

Another source of names of attorneys is *The Martindale-Hubbell Law Directory*. This directory provides a listing of attorneys. Specific information about these attorneys is also provided, including a rating system showing how other attorneys view their level of competence and integrity. This publication is available in law libraries, through local bar associations, and in some banks or legal offices.

Regardless of how highly recommended an attorney may be, you are the person who must make the final decision regarding who should represent your business. The question that you should ask is, "Do I have enough confidence in this person to want him or her to represent me and my business?

In order to find the answer to this question, you will need to set up interviews with several promising prospects. An initial session with an attorney may cost you a small fee, but some attorneys will spend time getting to know a prospective client without a cost involved.

You may wish to use the time in the initial meeting to talk about business needs in a general manner. During the discussion, it will become apparent whether a rapport has been established.

During the "give and take" of the initial interview, you should ask about the attorney's fee structure. Because many of the services your business will need will be long-term items, the attorney may not be able to quote flat fees. If your business will require extensive legal counsel, let it be known that you will expect an itemized monthly statement. Then, you will be able to monitor costs and make sure that they do not get out of hand. If expenses for a specific legal service are found to be rising, you'll be in a better position to call "time-out" to discuss the advisability of terminating the project.

Fees for collection work may be figured on a different basis than other legal matters. Usually, an attorney will charge a percentage of whatever is collected. In addition, the business will generally have to pay any court costs and out-of-pocket expenses the attorney might incur.

As a small business owner, you will need to budget for legal expenses. After all, legal expenses are as integral to your business as allocating funds for capital improvements or advertising. As you shop for an attorney, remember that you have every right to shop for legal fees that you can afford. The Supreme Court has said that it is illegal for bar associations to fix minimum fee schedules for attorneys.

Once your initial interview with an attorney is completed, you will know if the attorney impresses you as being capable and responsive to your needs. Even if this is the case, don't hand over all your legal work to this person immediately. Test the attorney and the firm's promptness and efficiency with a short-term project. Set up time frames or a series of deadlines to find out if workloads are handled on schedule. During this period, see if your attorney is accessible. Your phone calls should be answered within a reasonable time. However, don't expect to reach your attorney immediately. Usually, you will find that a good attorney is very busy.

Once you have made your decision and have selected the law firm and the attorney you think is right for you and your business, stick to your choice. It is not good to hop from one firm to another for different jobs. An attorney's services are most effective when they are coordinated under one roof. However, you may find that there are exceptions. For example, in the case of highly specialized legal matters, such as trademark and patent work, projects are often referred to attorneys who specialize in these areas. Usually, your attorney will refer your work to another firm, with your consent. In such cases, it is wise to give your attorney the go-ahead. After all, a good attorney will know the firm's limitations as well as its strengths. In addition, your attorney should know to whom such items should be referred.

Remember that as an owner/manager, you can get good value from a close working relationship with your attorney. In such cases, your attorney will be aware of the many aspects of the business and will be able to give quicker and more carefully reasoned opinions. Close knowledge of your trade customers, business customers, suppliers, and employees and their contractual relationships will help you improve your lawyer's services.

Despite every precaution, you may come to the conclusion that you have chosen the wrong attorney. Some of the signals are an attorney who appears inattentive or distracted, one who fails to meet deadlines, or who draws up contracts that turn out to be inadequate. On the other hand, you may have an attorney who bombards you with several reports a week on anything you may be remotely interested in. If this is the case, you may find that you are paying for a lot of busy work.

Some business people give an attorney his or her "walking papers" just because the attorney didn't come through with a total victory in court. These people have forgotten an important issue. Most litigation ends in compromise. Often both parties are somewhat dissatisfied with the outcome.

In seeking the right attorney, check all the externals—the size of the firm, personal impressions, and track records. Remember that equally important in this selection process is you, the prospective client. A clear focus on your needs and the services you require for you and your business will make your search and your ultimate selection a positive one. Once you have identified the right attorney for your business, you will be able to obtain assistance with the legal problems related to your business. One of the items that you will deal with is contracts.

WHAT IS A CONTRACT?

A contract is a mutual agreement made between two or more persons that is valid and enforceable by law. It does not have to be written in order to be legal. In fact, oral contracts can be enforced providing their terms can be established in a court of law. Sometimes, however, oral contracts can present problems. With oral contracts, it may be difficult to establish what has been agreed upon. Each party may be relying on personal memory and bias.

When money is involved, it is typical to put contracts in writing. In addition, the following conditions call for a written contract:

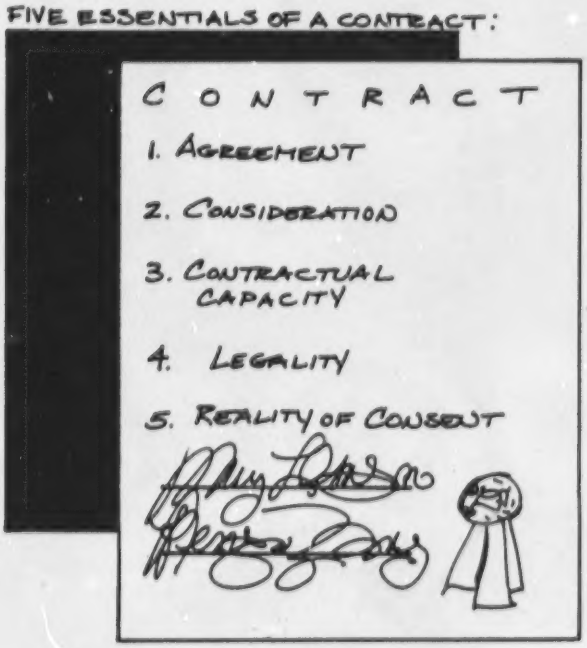
- Any contract for the sale of land or an interest in land
- Any contract that will not be performed within one year
- A promise by one person to pay the debts of another
- Any contract that involves the purchase of real property valued at $500 or more

In examining when to use written contracts, it is safest to use them in all but minor matters. This way, if there is a problem with the contract, the business person can spend time trying to get performance on an award for damages rather than arguing over the terms of the contract that were initially agreed upon.

As a small business owner/manager, you need to know the major requirements of a contract. These requirements cause the contract to be legal and binding. Knowing these requirements will increase your awareness of some of the problems that are encountered in the enforcement of contractual agreements. The major requirements of a contract are often called the five essentials of a contract.

WHAT ARE THE MAJOR ELEMENTS OF A CONTRACT?

The five essentials of a contract are (1) agreement, (2) consideration, (3) contractual capacity, (4) legality of purpose, and (5) reality of consent. Contracts that are enforceable by law have these five items.



The first and most important element of the contract is *agreement.* For agreement to exist, there must be a reasonably definite understanding between the parties. Agreement occurs under the following conditions:

1. An offer is made. (An offer is a proposal that expresses a desire to enter into a legally binding agreement.)

2. The offer is followed by acceptance. (Acceptance occurs when the party to whom an offer has been made agrees to the proposal.)

3. The offer and the acceptance create a reasonably definite understanding between the parties who are involved in the contract.

Some of the most important ingredients for *agreement* are intent to contract, reasonable definiteness, and communication. Let's take a closer look at these items.

Sometimes people talk business in exploratory terms. There is no agreement and no contract. In order for a contract to exist, the parties involved must intend to contract. This means that all parties must desire to enter the contract and to meet the terms of the contract.

In order for an agreement to exist, the offer has to be reasonably definite. This means that the terms have to be specific enough so that it can be determined when the parties to the contract have lived up to their promises.

Another item that is necessary for agreement is communication. In order to have a contract, an offer has to be communicated to the offeree.

A second requirement for a legal contract is *consideration.* Consideration is something of value that is given to the offeror by the offeree. What constitutes consideration? One of the ways in which the courts have attempted to answer this question is with the detrimental test.

Will the person bringing suit suffer a detriment (loss or damage) if the contract is not carried out? Has the person already suffered a loss? If the answer is yes, the courts will hold that consideration existed.

Another requirement of a legal contract is that of *contractual capacity.* All parties to the contract must have the ability to make legally binding agreements. Individuals who have the capacity to contract are known as competent parties.

Those who do not have the capacity to contract are classified as incompetent. They include persons who are mentally ill or insane, intoxicated by drugs or liquor, or under legal age.

Still another requirement of a contract is *legality of purpose.* Contracts in violation of the law are not enforceable. A contract must be legal in its objective. It must not be contrary to the interests of society in its formation, purpose, or performance.

The final requirement for a contract is *reality of consent.* This is missing when the agreement contains fraud, innocent misrepresentation, or mistakes.

It takes agreement, consideration, contractual capacity, legality, and reality of consent to make a contract. When all five factors are present, we have a contract. Without them, we do not have a contract.

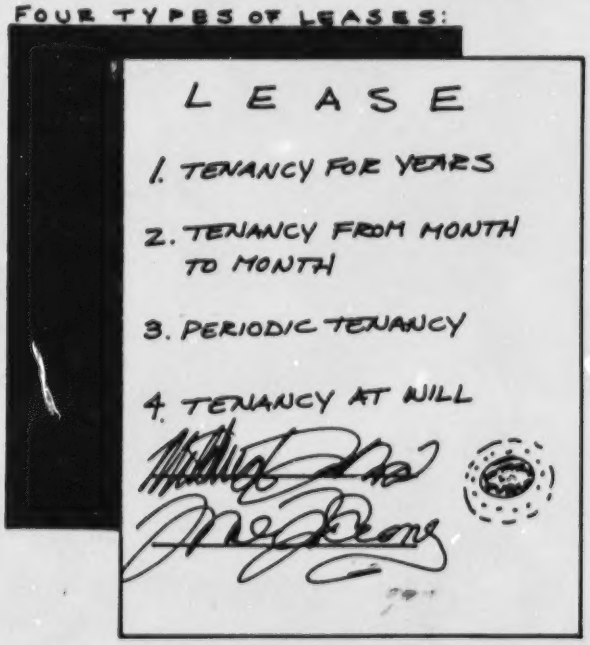
WHAT ARE THE MOST COMMON TYPES OF CONTRACTS?

The two most common types of contracts are lease contracts and sales contracts. At this point in time, you will have an opportunity to learn more about lease and sales contracts.

As you start your business, you will probably lease the site for the business rather than buy it. For this reason, it is important for you to become acquainted with leases and their terms.

WHAT IS A LEASE?

A lease is a special contract that establishes a relationship between a property owner and a tenant. A tenant (lessee) has possession of the real property of the property owner (lessor). Rent is the payment given by the tenant to the property owner. Many states have laws or statutes regarding these leases. In some states, if the leasing period is longer than one year, the contract must be written to be enforceable.



WHAT TYPES OF LEASES ARE AVAILABLE?

There are various types of leases that a business can sign. Selecting the "right" lease depends on the circumstances, type of business, and common leasing practices within the industry. There are four types of leases:

1. **Tenancy for years.** The site is leased for a definite period of time. The lease can last six months, one year, five years, or ninety-nine years.

2. **Tenancy from month-to-month.** The site is leased month by month, and rent is paid by the month.

3. **Periodic tenancy.** The site is leased for an indefinite period of time with rent due at specified intervals.

4. **Tenancy at will.** The site is leased for an indefinite period of time. The Lease can be continued indefinitely or can be terminated by either party.

WHAT SHOULD A LEASE INCLUDE?

Since a lease is a legal document, it is important that certain precautions be observed before the lease is signed. Examine the property thoroughly to make sure that it suits the purpose for which it is to be used. Make sure that the signatures are properly witnessed. Examine the lease thoroughly to make sure that it contains the following:

- No narrow restrictions on merchandise that may be sold or on services that may be provided
- Statements of the duration of the lease, the amount of rent, the date on which the rent is to be paid, and the penalty for late for nonpayment
- Arrangements for subleasing, subletting, and assignment to another merchant
- Provisions in case of fire or other hazards
- Mutual obligations concerning major and minor repairs
- Options and renewal arrangements[1]

WHY LEASE EQUIPMENT?

Often businesses lease more than the firm's premises. Even though leasing rates are usually higher than rates charged for purchasing the equipment on credit, many small firms lease equipment. Manufacturers very often lease machine tools and heavy equipment, including trucks. It is not uncommon to find service, wholesale, retail, and manufacturing firms leasing data processing equipment, photocopying equipment, and company cars.

Leasing has some very definite advantages because it—

- does not tie-up capital;
- eliminates the need for some types of insurance protection;
- saves taxes. Lease payments are tax-deductible;
- eliminates possession of outdated equipment and so forth. (When new models become available, most lease agreements

allow the lessee to exchange the equipment for the new models.);

- saves on maintenance costs since these costs are usually included in the terms of the lease.

WHAT ARE SALES CONTRACTS?

A distinction must be made between a sales contract and a contract to sell. The Uniform Commercial Code (UCC) states, "Contract for sale includes both a present sale of goods and a contract to sell goods at a future time. A sale consists in passing the title from the seller to the buyer for a price." A contract to sell means that the title of goods is to pass at a later time.

As a small business owner/manager, you will deal with a variety of sales contracts. These contracts may involve sales to customers or items that you intend to purchase. You may even work with a sales contract in order to purchase your own small business.

If you decide to purchase an existing small business, you will need to develop a sales contract. You may want to have your lawyer draw up the agreement. This will help to assure that it covers all essential points and that the agreement is understood by all parties.

If you purchase an existing business, you will want to have the following items covered in the agreement:

- A description of what is being sold
- The purchase price
- The method of payment
- A statement of how adjustments (such as inventory sold, rent, payroll, and insurance premiums) will be handled at the time of closing
- Buyer's assumption of contracts and liabilities
- Seller's warranties (such as warranty protection for the buyer against false statements of the seller, inaccurate financial data, or undisclosed liabilities)
- Seller's obligation and assumption of risk pending closing

- The covenant of the seller not to compete with the business
- The time, place, and procedures of closing

There are several things that you will want to remember if you are purchasing an existing small business. One of these is the fact that the seller and the buyer must comply with the bulk sales law of the state in which the transaction takes place. This law will help to protect the buyer of the business. It is designed to assure that the seller does not sell out the business, pocket the money from the sale, and disappear leaving the creditors unpaid.

As a result of the bulk sales law, the seller will need to furnish a sworn list of creditors to the buyer. The buyer will give notice to the creditors of the pending sale. If that does not happen, the seller's creditors could possibly be able to claim the personal property that the buyer has purchased.

The buyer of the business will want to take possession of the business as soon as possible after signing the contract. This will keep the seller from depleting the inventory or from creating ill will for the buyer as the business is taken over.

WHAT LAWS WILL AFFECT YOU?

The type of laws that you will have to obey as a small business owner will vary according to the type of firm that you own. One of the things that you will need to do as a small business owner is to check out the nature of the various laws that you will need to obey.

Regardless of the type of business that you have, you will probably need to obtain a taxpayer identification number. Your taxpayer identification number is your employer identification number. It must be shown on all of your business tax returns (such as IRS Schedule C) as well as on any tax-related documents and statements. If you are required to file an excise, alcohol, tobacco, firearms, or employment tax return, you must put your employer identification number on that return. If you incorporate your sole proprietorship or form a partnership, you must get a new employer identification number to use on returns of the new corporation or partnership.

To apply for an employer identification number, use Form SS-4, Application for Employer Identification Number. These forms are available from the Internal Revenue Service. In addition, you may wish to obtain the "Business Tax Kit" from the Internal Revenue Service to learn more about the various taxes that you will need to pay.

You may also find that the following checklist will be helpful to you in dealing with legal issues:

- Do you know what licenses and permits you need for your business?
- Do you know what business laws you will have to obey in your business?

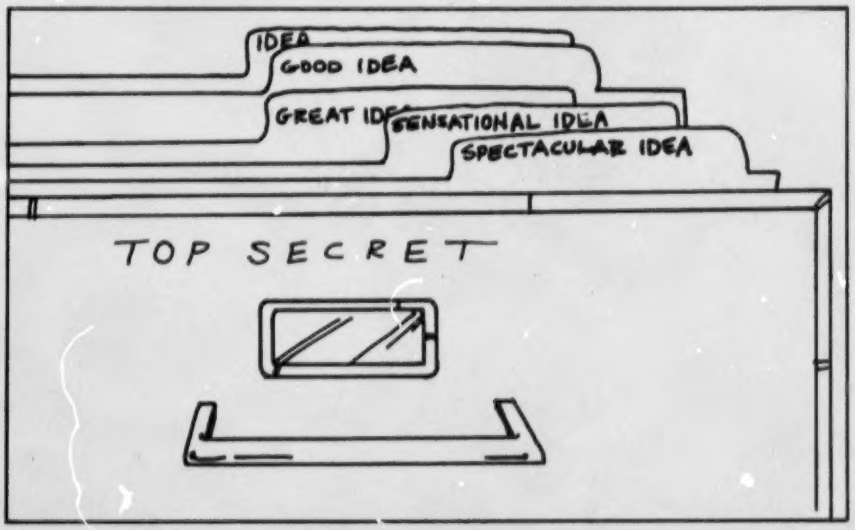
- Will your operations be subject to interstate commerce regulations? If so, do you know which ones?
- Do you know what police and health regulations apply to your business?
- Do you know a lawyer you can go to for advice and help with legal problems?
- Have you received advice from an attorney regarding your responsibilities under federal and state laws as well as local ordinances?
- Have you made application to the city or county clerk to register your business name? This may be necessary if you are doing business as a sole proprietor and using a name other than your legal name.
- Have you made application for the copy of your employer taxpayer identification number?
- Have you made application for your sales tax identification number? This is necessary for businesses that are required by law to collect sales taxes or that purchase merchandise that is for resale and not subject to sales tax.
- Have you made application for a State Unemployment Insurance Number? This is necessary for businesses that pay compensation, with the exception of remuneration of sole proprietors and partners.
- Have you made application for Worker's Compensation Insurance numbers and State Disability Insurance?
- Have you made application for licenses required by federal, state, and local legislation?
- In the case of a partnership, have you made copies of partnership agreements and other agreements between the partners?
- In the case of a corporation, do you have a copy of the corporate kit with stock certificates, seal, and articles of incorporation?
- Do you have copies of purchase agreements between suppliers and the business?
- Do you have copies of contracts between the business and its clients, plus other contracts related to the business?
- Do you have lists of property, serial numbers, and property value of items used in the business?

- Do you have lists of clients, with addresses and phone numbers?
- Do you have copies of insurance policies on the lives of partners, officers, liability on business premises, and all other kinds of insurance carried?
- Do you have Employee Compensation Records, including applications for employment, copies of W-4 Forms, plus Withholding Exemption Certificates?
- Do you have documents applicable to the particular industry and locality (for example, board of health permits, zoning variances, and so forth)?
- Are there any other legal items that will be necessary for your business? (If so, make a list of these items on a separate sheet of paper.)

By using this checklist, you should be able to identify the information that you will need for legal purposes. Now, let's take a look at another concept that is related to legal issues in business. That is the concept of protecting your ideas.

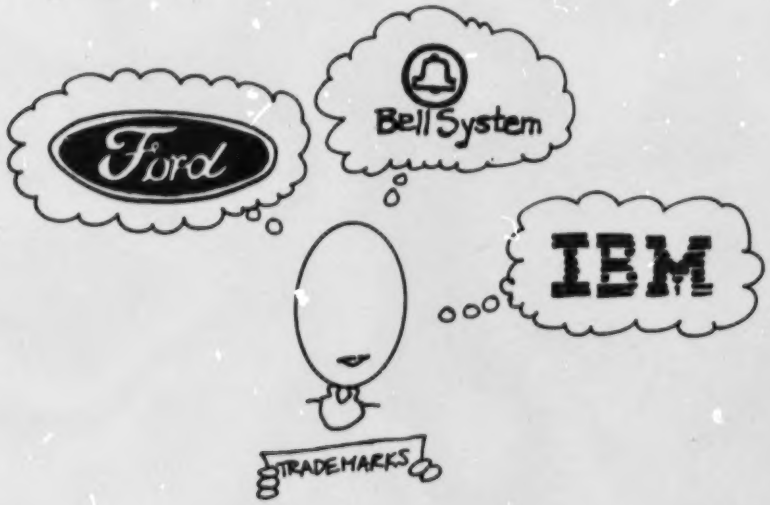
HOW DO YOU PROTECT YOUR IDEAS?

In the process of doing business, you may have an opportunity to originate a new idea for a product or process. If so, you may wish to take steps to protect your idea through patents, trademarks, service marks, or copyrights. Let's take a closer look at these items and how they can protect your ideas.



If you invent an item in the process of operating your business, you might want to have it patented. Patents may be obtained on new industrial or technical processes, machines, designs, or other items. A patent would provide exclusive rights to the inventor to make, use, or sell their particular invention for a period of years.

A trademark is a word, name, symbol, device (design), or a combination of these items that is used to identify a product. When a trademark is registered, that trademark is protected against use by others for a period of twenty years. The trademark is a device pointing distinctly to the origin or ownership of merchandise to which it is applied. The trademark is legally reserved to the exclusive use of the owner as maker or seller of the product.



Like a trademark, a service mark is a word (or words), design (or designs), or combinations of word(s) and design(s) used to advertise services. A service mark helps customers to distinguish the services of one firm from those of another. These marks are used to advertise banking, real estate, motel, or other services. Through such advertising, prospective customers become aware of your services. When they see your service mark, they associate it with a particular level of quality.

Literary and artistic work is protected through copyrights. Copyrights are effective for the life of the author plus an additional fifty years. As a small business owner/manager, you may desire to copyright material used in advertising. For example, your catalogs, brochures, or instruction sheets regarding products and services could be copyrighted.

Patents, trademarks, and service marks are issued by the Commissioner of Patents in the U.S. Department of Commerce. Trademark and service mark registrations are also offered in most states. Copyrights are processed through the Copyright Office of the Library of Congress in Washington, D.C.

ACTIVITIES

The following activities will assist you in learning more about dealing with legal issues.

INDIVIDUAL ACTIVITY — Review trade journals in the field to locate articles on major changes in legal issues that effect your business.

INDIVIDUAL ACTIVITY — Make a list of the local, state, and federal taxing agencies which will have an impact on your business.

INDIVIDUAL ACTIVITY — Design or locate any trademarks or service marks that will be used in your business.

GROUP ACTIVITY — Using individual activity number one or other information, have a group discussion regarding new legal issues which will have an impact on small business management.

INDIVIDUAL ACTIVITY — Design or locate any trademarks or service marks that will be used in your business. Find out the steps that are necessary to register these marks. Prepare a short report on these steps for presentation to the class.

CASE STUDY — Sandi Clinn has been thinking about starting her own business for some time. She has been working in a local tennis shop for several years and knows a great deal about the business operation.

Sandi has started looking for a business location and she has found that a local realtor has been very helpful. One of the places that she is considering is owned by another realtor. Sandi believes that she is getting expert advice and assistance. However, she has decided that she would like to secure the advice of an attorney regarding lease provisions.

Sandi has not utilized a lawyer previously. She isn't quite sure what procedures she should take in order to locate a lawyer.

Answer these questions on a separate piece of paper.

1. Outline a procedure for Sandi to use in order to locate a lawyer.

2. Today, many lawyers are advertising their services. Should Sandi use ads to select her lawyer? Why or why not?

ASSESSMENT

Directions. Read the following questions concerning dealing with legal issues. They are to help you check your knowledge about this topic. When you feel ready, ask your instructor to assess your knowledge of them.

1. Where can the small business owner find information regarding potential sources of legal problems?

2. What techniques can be used to reduce legal problems?

3. How can a small business person obtain assistance with legal problems?

4. Where can you go to find information on patents and trademarks? On copyrights? What kinds of protection do these registrations give the small business owner?

NOTES

[1]Wingate, I.W., and Sampson, H.E. *Retail Merchandising.* 8th ed. Cincinnati, OH: South-Western Publishing Co., 1975, p. 86.

We thank the above authors for permission to reprint from their work.

SOURCES USED TO DEVELOP THIS UNIT

Fisk, McKee; Mietus, Norbert; and Snapp, James. *Applied Business Law.* Cincinnati OH: South-Western Publishing Co., 1972.

Goodman, Kennard E., *Today's Business Law.* New York: Pitman Publishing Corporation, 1966.

Lewis, R. Duffy and J. Norman. *What Every Retailer Should Know About the Law.* New York: Fairchild Publications, 1963.

Myers, K.O. *The Law of Contracts.* Columbus, OH: Distributive Materials Lab., n.d.

For further information, consult the lists of additional sources in the *Resource Guide.*

Level 3

PACE

Unit 1. Understanding the Nature of Small Business

Unit 2. Determining Your Potential as an Entrepreneur

Unit 3. Developing the Business Plan

Unit 4. Obtaining Technical Assistance

Unit 5. Choosing the Type of Ownership

Unit 6. Planning the Marketing Strategy

Unit 7. Locating the Business

Unit 8. Financing the Business

Unit 9. Dealing with Legal Issues

Unit 10. Complying with Government Regulations

Unit 11. Managing the Business

Unit 12. Managing Human Resources

Unit 13. Promoting the Business

Unit 14. Managing Sales Efforts

Unit 15. Keeping the Business Records

Unit 16. Managing the Finances

Unit 17. Managing Customer Credit and Collections

Unit 18. Protecting the Business

Resource Guide

Instructors' Guide

Units on the above entrepreneurship topics are available at the following three levels:

- Level 1 helps you understand the creation and operation of a business
- Level 2 prepares you to plan for a business in your future
- Level 3 guides you in starting and managing your own business

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